



March 17, 1967

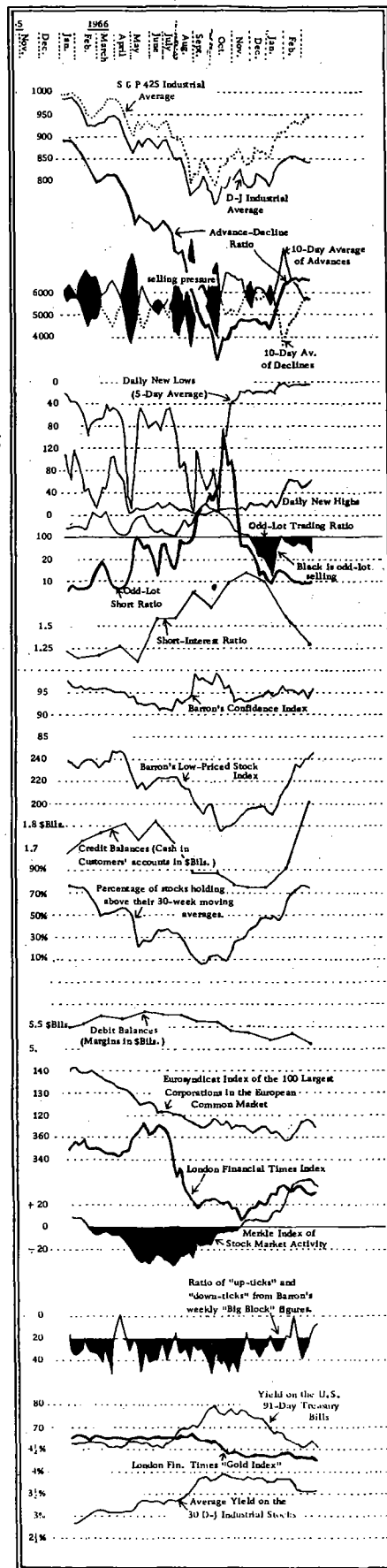
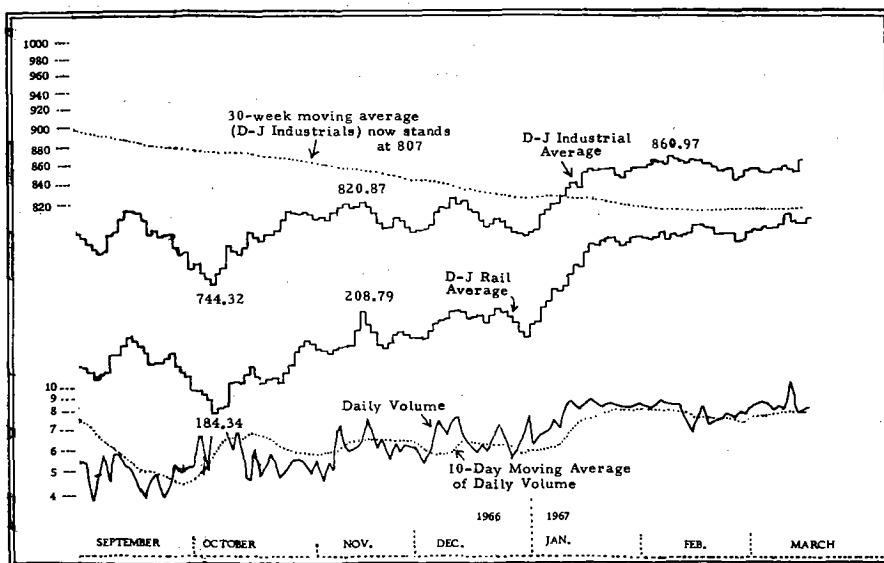
Letter 352

THE MARKET: It is now generally conceded that the government is pulling out "all the stops" in an attempt to reverse a mounting trend of bearish business statistics. While President Johnson states (for public consumption) that he is gratified at the obvious "cooling off" of the economy, the action of the various Federal agencies indicate that there is now far too much cooling off to suit the Administration.

In early 1966 amid a background of glowing business statistics and forecasts, the Averages touched historic highs. At the time it was widely held that "1000 on the Dow" was a figure which would be achieved within a matter of a few days or weeks. But the market chose instead to embark on a major decline. In May, 1966, the Industrials and Rails signalled a primary bear market. During almost all of 1966 we were promised that business would stay good, despite the market downturn. Presidential advisors as highly-placed as Gardner Ackley stated that no recession was in sight for 1967. But the market can see further than President Johnson, the Fed, and all the Presidential advisors together. We are now witnessing the early part of an economic decline, a decline which the Averages forecast over a year ago. The first part of the bear market lasted from February to October, 1966.

From the October, 1966 low of 744.32, a major upward correction took the Industrial Average to 860.97 (February 8), this despite a torrent of almost uniformly poor business news. A shallow decline followed, accompanied by various government announcements regarding easing of corporate taxes and the reinstatement of all types of monetary stimulants. In his page 1 column for the Wall Street Journal, George Shea (March 13) noted the failure, so far, of the Government's stimulants to work on the economy. In a wry closing to his piece, Shea commented: "Altogether, it may be said that so far the shoring-up measures have been principally reflected in stock market celebrations."

For my part, I have already observed that the Government has pulled out all the stops in an almost frenzied attempt to "get things going again." It should be remembered that most of the new Government stimulants were announced after the February 8 (860.97) peak in the Dow. The rally to the February 8 high, in my opinion, represented the market's appraisal of the best that could be seen ahead for business and corporate profits. It will be most interesting to see whether (following all the recent Government "pep pills") the Dow can push on to new highs. If it cannot, I believe the market will be saying that the Government's efforts are due to fail. The market will then be saying that the primary bear forces are stronger than all the manipulations, arrangements and "hypos" that Washington can come forth with.



Page 2 Here is something else I have been watching. It appears that each successive lower peak in Industrials brings in more volume. But there is a difference between volume which takes the market to new highs and volume which "churns" under a previous peak. I have always accepted the latter as indicative of distribution. For example, average volume during January and early February, 1967, with the Industrial Average less than half-way back to its 1966 high, was running around 10 million shares per day. This was considerably more volume than the 8.5 million shares per day which appeared at the February, 1966 all-time highs.

Following a decline into late February, 1967, Industrials again pushed up. On February 10, in response to news of the reactivation of the 7% corporate investment credits, Industrials surged over 13 points but closed up around 4 points, still well under the February 8 peak of 860.97. Volume for the day was 14.9 million shares, second biggest day in the history of the N.Y.S.E. On a cold reading of the facts so far, with all the economic stimulents and announcements of the past few weeks, with an easing of interest rates, to the accompaniment of some of the heaviest volume ever seen on the Exchange, the Industrials have failed (so far) to better their February 8 high.

SUNDRY THOUGHTS: The machinations and frenzied efforts of our government as it tries to keep the economy on "even keel" are a sight to behold. Push long-term interest rates down, keep short-term interest rates at around 4.5%, swap dollars for foreign currencies, remove investment credits for industry, reinstate them, hold up crop prices, publish guidelines for prices, ignore the guidelines if the economy turns soft, protect certain industries with tariffs, change the budget figures to show a smaller deficit if the deficit looks too high, on and on, the "manipulation list" is almost endless. And it all seems to work while the primary trend is bullish. Mistakes and acts of stupidity are usually bailed out by rising prices, optimism and inflation during a bull market. But ultimately the tide starts running out.

Have you ever seen two boys building a sandcastle on the beach? After a while the waves start touching the castle and the little sand walls begin to crumble. The boys call for help, and perhaps dad and three older brothers and sisters rush to fortify the castle walls. The extra hands seem to be the answer—for a while. Then the tide starts coming in earnest, and 100 extra hands would not help. The force of the tide is irresistible, and in a few minutes the little castle is washed flat. It was exciting. For a brief span everyone almost believed that the castle would withstand the tide. But no sand castle ever built has stood against the ocean's force for long. Ocean's are simply too strong.

It seems to me that we are watching the same kind of psychology and thinking today. As I study the news I have the strange feeling that the walls are springing leaks. Autos, tools, appliances, housing, railway car orders are all slumping. Suddenly it looks like housing is picking up a bit, but now the textile business is sagging. The bright spots are harder and harder to find, and when it looks as if you have come up with a piece of good news—why two other pieces of bad news pop up to take its place.

A few factors are worth considering at this point. One is that over the past five months unit labor costs have risen at an unprecedented annualized rate of 9.6%. Coming labor-management negotiations give every indication that the rate is going even higher. This is occurring in the face of a slackening in the rate of sales growth in the private sector of the economy. The result must be a further squeeze on corporate profits. It is in recognition of this and other factors that the government has rushed in to try to reverse the trend. I take the "rush" to be the government's tacit admission that the economy is now in recession.

The market has accepted the government's latest series of actions as a sure-fire mechanism calculated to make the business outlook bullish again. But I do not see how more money or easier money or a reinstatement of the 7% tax credits for equipment are going to reverse the profit squeeze. Nor am I convinced that consumers, who are now over their heads in "inventories" of appliances and equipment of every variety, will rush to spend more money simply because there is more money available. There is no guarantee that consumers are not going to continue their stepped-up saving policies, policies which have become increasingly apparent over recent months. "You can lead a horse to water," runs the old adage, "but you can't make him drink."

There is no doubt that the test is now on and that the stock market has risen in an effort to partially discount that test's possible success. The test is whether the government can reverse a cycle of declining consumer spending and declining corporate profits. The period ahead will, in many ways, be one of the most fascinating in American financial annals.

As if to underline the dangerous "split-personality" of this market, it is well to note that on March 10 the Rail Average advanced to a new recovery high of 234.18. On the same day the Utility Average sank to a new low for the year. Rails may be considered the "speculative component" of the market while Utilities may be taken as the investment component. It is also significant that Utilities broke to new lows in the face of easing money rates. In other words, the current decline in the Utility Average cannot be excused on the basis that "Utilities are merely acting as 'money stocks' or 'interest rate' stocks." It should be remembered that the Utility Average led the market down during 1965-66 and the Utility was the first Average to turn up prior to the 1966 October bottom.

STRANGE THINGS ARE HAPPENING: I keep stressing the action of the D-J Industrial Average, not necessarily because the Dow Theory is based in large part on the action of this Average, but because I believe that what the Dow is now doing is extremely important. The 30 stocks in the Dow represent over 40% of the value of the New York Stock Exchange. Taken in total, these 30 giant corporate entities reach into almost every fiber of the American economy, their annual profits are staggering, they employ millions of American workers. The fact is that a persistent trend in the 30 Dow stocks must sooner or later exert its effect on the rest of the market and the rest of the nation. The Dow Industrial Average is too "big," too all-encompassing to be written off as so many analysts are now doing.

So far, the picture is this. The D-J Industrial and Rail Average gave the signal for a primary bear market in early 1966. An important upward correction began in October, 1966, following the 250 point drop in the Dow. According to Dow Theory, a movement terminates at the point where the two Averages (Industrials and Rails) register their last joint highs (or lows). On this basis, the rally which began in October ended on February 8, 1967 (unless, of course, a future rise takes both Industrials and Rails to new highs for the year).

The little decline since the February 8 high has been minor and not particularly impressive. On the fact of it, most analysts have "written it off" as merely a downward jiggle preparatory to ultimate new recovery highs. But here is what impresses me. All during the bull market of 1949 to 1966 it was the big Dow stocks that led the market to successive new highs. In other words, investment-grade stocks backed by investment-grade money led the way. In late 1965 and early 1966 this changed. The market turned extremely speculative in 1966 with all rallies being led by violent activity in speculative, "glamor" and low-priced stocks. The Dow stocks remained persistently and outstandingly weak during these "blow-offs." In 1966, when the Dow Industrial Average finally collapsed, the speculative stocks broke with the Dow.

Now, in 1967, the speculative fever in the market is higher than ever. But what of the Dow stocks, what are they doing while the junk stocks boil? The best test is relative strength. We want to see how the Dow stocks are doing in relation to the rest of the market. If

the Dow stocks were only suffering the same percentage of decline as the rest of the market (as represented by the Standard & Poor 500 Average) or if the Dow stocks were actually losing less (in percentages) than the S & P 500, I would call the action good. But this has not been the case.

I have gone through each of the Dow stocks on a long-term and a short-term basis (perhaps the short-term of 1967 performance is more important than the long term at this juncture). In the great majority of cases, the Dow stocks have acted worse than the general market. I consider this a distinctly negative omen for the market. I cannot accept the fact that low-priced and speculative shares "put on a show" while the Dow stocks lag as being bullish. It smacks of investment-grade distribution, and I think it will ultimately lead to a resumption of the primary bear trend. Here is the relative strength record of the 30 Dow stocks. Of these, 21 are acting poorly on a relative strength basis, one (Johns-Manville is doubtful) and 8 are acting better than the market. Swift and Westinghouse have been the stars of the Dow during 1967.

Allied Chemical...Relative strength line (RS) rose from a Nov. low to a Feb. high, now declining again. The Nov. low was the lowest in a decade.

Alcoa...RS poor, now at new low for the year.

American Can...RS may be turning up from a low for the year set in February.

American Telephone...RS rising from a low for the year set in early February but looking better.

American Tobacco...RS moving sideways since 1964, near low for the year now.

Anaconda...RS sideways since November, following a three-year rise.

Bethlehem Steel...RS near lowest level in a decade.

Chrysler...After dropping to the lowest level since 1963, RS on this stock is now moving sideways above the extreme low of last November.

duPont...RS at the low of the last dozen years.

Eastman Kodak...The star of the Dow, RS line at highest level in years and still rising.

General Electric...RS breaking down badly and now at its lowest level since 1954.

General Foods...RS sagging to a low for the year.

General Motors...RS line at approximately last December's low, which level represented the lowest RS level since 1962.

Goodyear...RS just off its low for the year, following a persistent sag since January of this year.

International Harvester...RS at a low for the year and at the lowest point since early 1965.

International Nickel...RS still in a long, gradually rising trend, a trend for the better which started in early 1964.

International Paper...RS now at a low for the year and the lowest level in a decade.

Johns Manville...RS still within the rising trend which started in 1966, but since mid-January the RS has been breaking down in a minor way.

Owens-Illinois...RS flat since last October but still within long-term rising trend which started in 1965.

Proctor & Gamble...RS flat since last October but still within longer term rising trend which started in 1965.

Sears...RS near low for the year and well within long-term declining RS trend which started in 1965.

Standard Oil of California...RS at low for the year and lowest level since 1962.

Standard Oil of Jersey...RS at low for the year and lowest level since 1962.

Swift...RS bullish, having rallied sharply and steadily since the October, 1966 low.

Texaco...RS flat or declining slightly since last October.

Union Carbide...Like duPont, UK's RS has been in a major slump. RS is now at about the low for the year and lower than at any time since the 1940's.

United Aircraft...RS is a rising trend since November, 1966.

U.S. Steel...RS still well within the major collapse in RS which started in 1959.

Westinghouse...One of the best of the Dow stocks with RS rising since September of 1965.

Woolworth...RS declining on a short-term basis during 1967 so far, and holding within the long-term RS decline which began in 1962.

So that is the story on the 30 investment-grade Dow stocks. Many veteran analysts are calling this a "schizophrenic market," a market which is being held up by speculative hopes and wild speculation. But one thing is certain. And that is that this is a market devoid of investment-grade leadership. For the blue-chip companies, the companies which tend to be the bellwethers of the future trend of American profits, are in the doldrums. Day after day we have seen the market start up with high hopes for the blue chips, only to see them sold off at or near the close. It is an extraordinary performance, and, I believe, an unhealthy one.

THE BATTLE LINE: The montage on Page 4, picked from last week's Automotive News and New York Times points up rather dramatically what is happening across the nation. It is obvious that those who are now speculating in the stock market are looking "across the valley" to the other side of the hill. Today's buyers are writing off the possibility that this is a primary bear market. They are dismissing the business news as "a temporary phenomenon," and they are convinced that government efforts will turn the business and profits picture around during late 1967 and 1968. Therein lies the dilemma and the battle line.

Page 4 If we are in a primary bear market (as I believe we are), then the far side of the valley (or business in the second half of 1967 and 1968) is going to be a great disappointment. Those buying stock now for a turnaround in the economy later this year are going to be wrong.

So far, I have noticed that almost all the actual news is poorer than expected. The major portion of the optimistic "news" consists of reports of Government stimulants and the hopes and expectations of what these stimulants are supposed to do. In other words, the facts are bearish and the expectations are bullish. The market's rise is based on the theory that the hopes will materialize. If my thesis is correct, if we are in a primary bear market, the hopes are not going to turn out the way the "hoppers" are expecting.

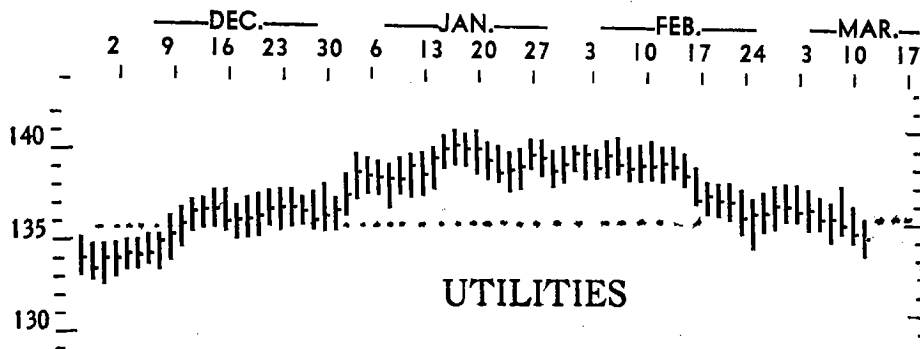


CHART OF THE WEEK: Above we see the daily chart of the D-J Utility Average (from the Wall Street Journal). The Utilities have broken off their shelf of December to March and are sagging steadily to new lows for the year. Over the past few years the Utility Average has had a habit of leading the market during impending major advances or declines. It may well be doing that again now. Certainly, a market which finds Utilities in a pronounced downtrend can hardly be called a "safe" market. It is a market in which the highest-grade D-J index is under persistent liquidation.

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NOTE: My friends Samson Coslow (publisher of Indicator Digest) and Harry D. Shultz (the Harry Shultz Letter and author of the book "Bear Markets") have come out with a new book entitled "A Treasury of Wall Street Wisdom." I consider this an excellent and long-needed addition to market literature. The book is divided into five major parts, each dealing with a different approach to the market (i.e., Dow Theory, wisdom of the twenties, wisdom of the thirties, etc.). The book is made up of actual quotes and articles from famous stock market practitioners, and it is the result of much time and research on the part of the two editors. I have agreed to carry the book and offer it to subscribers postpaid at \$6.95. (Hard cover, 392 pages). Please make checks out to Richard Russell Associates.

POINT & FIGURE: P & F charts have the advantage of "condensation." They show only movement, not time. This chart (from Chartcraft, Larchmont, N.Y.) shows the Dow from 1965 to the present. Each vertical box represents a 5-point move. All O's represent declines, all X's represent advances. Each time the Dow travels 15 points or more in a reverse direction, a new vertical series is started. This is known as a 15-point reversal chart with each individual box representing a movement of 5 points or more.

Note the "support" at the 835 level, which has now been tested twice. The recent peak is shown by an X at the 865 level. A rise to 860 would reverse the long descending or bearish resistance trendline from the 1966 high. A rise to 870 would push the Dow clear of the whole recent "congestion area," an area which contained the highest volume in Exchange history. Conversely, to break the chart down it would require a move to 830 on an hourly basis, as such a movement would put a zero below the two zeros at 835, thus reversing the intermediate trend on this chart to the bear side. I find P & F charts particularly helpful in confused situations such as the present.

Sales Fall to 5-Year Low; AMC Shows Only Gain

By Douglas A. Condra
Staff Writer

THAT spring selling boom can start any time now as far as U. S. new-car dealers are concerned, because things aren't getting any better this winter. The selling picture continued to grow bleaker in late February, as final industry figures showed a 1.7% new-car sales at their

was the highest 10-day rate since the final period of last December. However, the late-February daily rate in 1966 was 34,904.

AMERICAN MOTORS' price cuts on its compact American were in effect during the month-end period, and they spurred the company's sales to their highest point of the calendar year.

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Business Spending in U.S. To Slacken, Survey Finds

Government Report Points to Slowdown in Outlays for Plants and Equipment in First Half, With Rise Later in '67

By EILEEN SHANAHAN
Special to The New York Times

WASHINGTON, March 8—Business spending on new plants and equipment was added today to the lengthening list of signs of a general slowdown in the economy this year.

It was not immediately clear, however, whether the prospective sluggishness in business investment would be considered

Textile Sales Lag Is Cited by Stevens

By ISADORE BARMASH
Although J. P. Stevens & Co., Inc., has recently noted improved demand in some areas of its business, "it cannot be said at this time that there has been any general revival in market activity," Robert T. Stevens, president and chief executive officer, told shareholders at the annual meeting here yesterday.

RAIL CAR ORDERS DECLINE SHARPLY

Sign of Intensified Shortage Perturbs Government

Special to The New York Times
WASHINGTON, March 7—The precipitous decline in new orders for freight cars and locomotives, largely a result of the suspension last year of the 7 per cent investment tax credit, has surprised and worried the Government.

